

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 79 of 1988

For Approval and Signature:

Hon'ble MR.JUSTICE A.R.DAVE
and
Hon'ble MR.JUSTICE D.A.MEHTA

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1. Whether Reporters of Local Papers may be allowed : NO
to see the judgements?
 2. To be referred to the Reporter or not? : NO
 3. Whether Their Lordships wish to see the fair copy : NO
of the judgement?
 4. Whether this case involves a substantial question : NO
of law as to the interpretation of the Constitution
of India, 1950 of any Order made thereunder?
 5. Whether it is to be circulated to the concerned : NO
Magistrate/Magistrates, Judge/Judges, Tribunal/Tribunals?

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COMMISSIONER OF INCOME TAX

Versus

AMORA CHEMICALS PVT. LTD.

Appearance:

1. INCOME TAX REFERENCE No. 79 of 1988
MR BB NAIK for the Petitioner
MR RK PATEL for the Respondent

CORAM : MR.JUSTICE A.R.DAVE
and
MR.JUSTICE D.A.MEHTA

Date of decision: 28/08/2002

ORAL JUDGEMENT

This is a reference at the instance of the Commissioner of Income-tax, Baroda, for Assessment Years 1979-80, 1980-81 and 1981-82. The relevant accounting periods are Financial Years 1978-79, 1979-80 and 1980-81, respectively.

2. The Income Tax Appellate Tribunal, Ahmedabad Bench 'B', has referred the following two questions for the opinion of this Court :

"1. Whether, on the facts and circumstances of the case, the rental income from the Bank of Baroda was taxable under the head "business income" or "income from other sources"?

2. Whether, on the facts and circumstances of the case, the interest difference on the extra amount of Rs. 2,50,000/- could be allowed as a deduction?"

3. We have heard Mr. B.B. Naik, learned Standing Counsel appearing on behalf of the applicant revenue and Mr. R.K. Patel, Advocate, appearing on behalf of the respondent company.

4. The facts, briefly stated, are that on 1st July 1978, the assessee company entered into an agreement with L.M. Patel and B.M. Patel (HUF) whereunder a portion of the building known as 'Suraj Plaza' was taken on lease at a monthly rent of Rs. 9,970/-. It appears that the building was constructed partially and certain other floors were yet to be constructed. As per terms of the agreement, the assessee company was to advance a sum of Rs. 6 lacs as loan to L.M. Patel and B.M. Patel (HUF) so as to enable the said HUF to construct other floors of the same building. The agreement further provided that the loan was to carry interest at the rate of 6% p.a. However, in fact, the assessee company advanced loan of Rs. 8.50 lacs instead of Rs. 6 lacs and thus resulting in additional loan to the tune of Rs. 2.50 lacs.

5. The Income-tax Officer came to the conclusion that the assessee company had rented out the leased premises to Bank of Baroda and the said activity resulted in the assessee company receiving rental income as "income from other sources". For arriving at this

conclusion, the ITO primarily relied upon the object clause of the Memorandum of Association, as, according to the ITO, the said clause did not permit the assessee company to carry on business of hiring out properties. Insofar as the payment of interest was concerned, the ITO found that the assessee company had borrowed funds from bank at the rate of 15% and had advanced the amount of Rs. 8.50 lacs to the HUF out of the aforesaid funds. Thus, according to the ITO, the differential rate of interest, that is, 9%, was not allowable in hands of the assessee company as a deductible item of expenditure in relation to the additional amount of Rs. 2.50 lacs advanced as loan to the HUF.

6. The assessee company preferred appeal before the CIT (Appeals), who, for the reasons stated in his order, held that the entire activity of obtaining partially constructed premises from the HUF on lease and hiring out it to Bank of Baroda constituted business activity of the assessee. It was further held by the CIT (Appeals) that the additional amount at the same rate of interest was advanced to the HUF by the assessee company on account of commercial expediency.

7. The revenue preferred appeal before the Tribunal against the aforesaid order of CIT (Appeals). There was difference of opinion amongst the members, who originally heard the appeal. The Judicial Member upheld the view of the CIT (Appeals) while the Accountant Member allowed the departmental appeal and restored the order of the ITO. Accordingly, the matter was referred to third Member by the President of the Tribunal under sec. 255(4) of the Income-tax Act, 1961, and the following two questions were assigned to the third Member for decision :

"1. Whether the rent received by the assessee
from the bank was business income?

2. Whether the interest difference on the
extra amount of Rs. 2,50,000/- can be
allowed as deduction?"

8. The order of the third Member has taken into consideration the figures of rent received and rent paid by the assessee company for all the three Assessment Years, which are as follows :

Assessment Year	Rent Recd.	Rent paid
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1979-80	4,29,427	1,36,463
1980-81	8,49,672	2,99,852
1981-82	8,49,351	3,23,019

The third Member has taken into consideration clause 8 of the Memorandum of Association of the assessee company as it existed and come to the conclusion that the same was wide enough to take within its sweep the activity carried on by the assessee company so as to hold that rental income received from Bank of Baroda would fall under the head "income from profits and gains of business or profession". The order has further taken into consideration the fact that, the moment statutory auditors had raised a doubt about the object clause, the assessee company had taken steps to amend the relevant clause by passing appropriate resolution in the ordinary Annual General Meeting and the said amendment was approved by the Company Law Board on 29th August 1981. For the purposes of holding that the assessee company was carrying on business, it has been found by the Tribunal that the assessee company was not having surplus funds to invest and hence it had borrowed money from the bank so as to earn rental income after obtaining the property on lease. The Tribunal has further found that once cumulative activities of the assessee company were taken into consideration, namely, the fact that after obtaining the property on lease, certain alterations and decorations were carried out in the premises, a director was specifically entrusted to look after the upkeep of the building etc., it was apparent that the activities of the assessee company constituted business and the income earned by way of rent had to be assessed as income from business.

9. In relation to the second issue regarding interest, the Tribunal came to the conclusion that, though the agreement between the assessee company and the HUF was for advancing only Rs. 6 lacs, the advancing of further amount of Rs. 2.50 lacs was out of commercial expediency and the payment of interest had to be considered from the angle of a businessman. It has been further found by the Tribunal that the additional funds were advanced to the HUF so as to enable the HUF to complete construction of additional floors, which were to be made available to the assessee company at the same monthly rent, which was stipulated in relation to floors which had already been obtained on lease. Thus, it has

been found that the funds were granted to the HUF in the business interest of the assessee company and no portion of interest paid by the assessee company could be disallowed.

10. Having heard both these parties and after taking into consideration the orders of the Tribunal, we find that the view expressed by the majority does not require any interference. It is apparent that the Tribunal has taken into consideration all the relevant factors and applied the law in correct perspective on the basis of facts and evidence, which have come on record. Nothing has been pointed out on behalf of the applicant revenue so as to enable this Court to take any other view of the matter. The figures of rent received and the rent paid by the assessee company, as reproduced hereinbefore, go to establish clearly that the assessee had undertaken a business venture and it was only because of the systematic activities that the assessee company carried on, that it was in a position to earn such a handsome rent after paying rent at a lower rate.

11. In light of what is stated hereinbefore, the questions referred to us are answered as follows :

Answer to Question No. 1 is in the affirmative, that is to say, the rental income from Bank of Baroda was taxable under the head "business income" and not "income from other sources". Answer to Question No. 2 is in the affirmative, that is to say, the interest difference on the extra amount of Rs. 2.50 lacs was rightly allowed as a deduction. Both the questions are, therefore, answered in favour of the assessee and against the revenue.

The reference stands disposed of accordingly.
There shall be no order as to costs.

(A.R. Dave, J.)

(D.A. Mehta, J.)

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